THE NATIONAL CITY BANK OF NEW YORK

1934

Economic Conditions
Governmental Finance
United States Securities

New York, October, 1934

General Business Conditions

TRADE reports have been better during September, and those who have been hoping for a moderate pick-up in industrial activity during the Fall are encouraged accordingly. Retail trade began to improve in the latter part of August, and in department stores and variety stores generally the gains were vigorous enough to make that month the best of the year to date, allowing for seasonal factors in the comparison. The Federal Reserve Board's adjusted index of department store sales, which had declined from 77 in May to 73 in July (1923-25 average=100), recovered to 79. According to preliminary reports, September figures will show that the improvement has been maintained. For the larger retailing organizations estimated sales gains over last year run from 10 per cent upward, in dollars, and with prices on September 1 about 6 per cent higher, according to the Fairchild retail index, the figures signify a larger movement of merchandise.

This showing is in line with the expectations of some of the large merchandising concerns, and while it is due in part to cooler weather bringing in buying which had been deferred during the heat wave, it also is based upon improved consumer buying power. An analysis was made in the last issue of this Letter which indicated that despite drouth losses the farmers' cash income available for Fall trade would be larger than a year ago, and relief and other expenditures putting Government money directly into consumers' hands reached a new high point during the month.

Moreover, the breaking of the drouth, with heavy rainfall over most of the affected area, has been helpful both in fact and sentiment. The rains came too late to be of value to the grain crops, except possibly late corn, but they have started grass growing again in the pastures, and the prospect for late forage crops is materially improved. They also supply the moisture needed for planting Winter wheat and rye and bringing them to a stand, and have made a beginning, though naturally only a beginning, toward repairing the deficiency of subsoil moisture.

Another factor favorable to retail improvement has been the declining tendency in finished goods prices, which has persisted through the Summer. The Fairchild index, to which reference has been made, shows a drop of 2.6 per cent since last April, while in the same period prices of raw materials as reported by the Bureau of Labor Statistics have advanced 10 per cent and prices of farm products 24.2 per cent. These converging movements, narrowing a disparity which has penalized the raw material producer, obviously aid in restoring his purchasing power, and are helpful to trade. To be sure, the situation invites the comment that the narrowing of the spread must come out of the earnings of the manufacturer and distributor unless it is accomplished by reducing costs, and thus is not an unqualified benefit at a time when earnings are needed to restore the economic equilibrium, and when the tendency in costs is all the other way.

On the basis of the factors cited there was reason to expect a seasonal improvement in trade, despite the obvious handicaps in the way of any broad business expansion. It has been demonstrated several times during the depression that business in goods of everyday use can make an impressive upswing after a period of quietness or recession, without much support from the heavy industries, for there is constant need to replace such goods, and in one way or another the purchasing power is found to keep consumers supplied with them The present upturn is of this character.

Industrial Operations at Low of Year

Thus far the retail improvement has lacked the support of a pick-up in industrial operations and the increased employment that would go with it, except in purely seasonal lines. On the contrary, the general indexes of industrial activity, adjusted for seasonal influences. have dropped to a new low level during September. Some of these indexes are now lower than at

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the bottom of the recession last Fall, and therefore represent the lowest point in productive activity since the early Spring of 1933. However, the textile strike, enforcing curtailment in the group of industries which usually give Fall expansion its main impetus, has been the chief factor in the month's decline, and now that the strike is ended the textile mills should make a compensating gain in operations, and lift the October indexes accordingly. Textile mills had been curtailing for about four months prior to the strike, and had done a great deal to get the inventory situation in order.

A moderate improvement has likewise appeared in the steel industry. The rise in operations from the low point of 18.4 per cent of capacity to 24.2 in the last week of September is not impressive in extent, but in percentage it is more than the usual seasonal amount. Steel production was above consumption for several months in the Spring, but the converse has been true since the end of June, and gradually stocks are being absorbed. Meanwhile the chief sustaining factors are purchases for Government construction and miscellaneous demands. The extent of the Fall recovery in steel is naturally uncertain, and will depend principally upon the policies of the automobile manufacturers with respect to buying for 1935 models.

Automobile production has declined considerably, as usual toward the end of the season, while dealers work off their 1934 stocks and manufacturers prepare for the changeover. August sales of passenger cars were reduced by more than the usual seasonal percentage below July, but continued to run above a year ago, and preliminary figures from some companies indicate that September sales have held nearly even with August, whereas the normal trend is downward. This is another reflection of the better buying power evident in the retail stores.

Expectations Continue Conservative

On the whole the business situation thus described is as good as business men generally expected. It indicates that the extreme pessimism entertained in some quarters with respect to Fall trade was unwarranted, and therefore holds promise of a Fall improvement in the consumers' goods section of industry. On the other hand, hopes of vigorous recovery that would include the construction and other capital goods industries are not being entertained.

The totals of construction contracts awarded during the last quarter of the year are likely to be a disappointment. Privately financed contracts placed during August were below the low level of one year ago, and the total awards including public projects were but 13.4 per cent larger. In the first half of September the gain over last year was cut to 2.7 per cent. The figures in the last three months of 1933 were swollen by Government awards, and according to the Dodge calculations aggregated $515,000,000, which was 41 per cent of the year's total. There is no probability of this figure being equalled this year. The modernization work made possible by the Federal Housing program, with its partial guarantee of bank loans made for that purpose, will add to the totals. But while this is a helpful and businesslike plan, well devised to increase employment and improve the country's housing, its contribution toward lifting the building industry back to the peak from which it has fallen will of course be relatively modest.

With respect to equipment and machinery industries, the unfavorable turn in railroad earnings during the past few months, and the increased costs put upon the roads by the new pension act and the restoration of wages to the pre-depression level, give a plain indication that they can buy no more than their minimum necessities. The attitude of the industries generally is similar, holding that neither earnings nor business prospects justify plans for expansion.

It is plain that the chief lack in the business situation is the lack of confidence in the ability to carry on trade and industry at a profit. The problem of how to make goods at present costs that can be sold at prices which people can pay is oppressing all the manufacturing industries. There is continuing uncertainty as to how Governmental policies will affect business. The evident prospect that unemployment during the coming Winter will be as severe as it was last Winter, requiring relief expenditures which will postpone the time when the budget can be balanced, keeps fiscal and monetary uncertainties alive. The proposals to supplement private economic activity by Government operations discourage private enterprise in a degree that may offset or exceed the stimulus given by the Government measures, and the budget is involved in these proposals also. Finally a growing dissatisfaction has been apparent with the results of the wage and price fixing and other changes in economic relationships made by overhead authority. It is certain that the economic system was in disorder and relationships within it unbalanced, but the experience with the measures taken to bring them back into balance has not been reassuring, for they have left a residue of labor troubles, of costs and prices out of line with buying power, and of general confusion and uncertainty which at this time is evidently a serious handicap to recovery.

Crops and Markets

There have been no developments in the agricultural situation during the month to require modification of the statement of farm

income given in the last issue of this Letter, in which estimates of the Department of Agriculture were quoted to show that the cash income of the farmer in the second half year would be higher than in the same period last year by about $400,000,000 or 13 per cent. The A.A.A. has greatly speeded up the disbursement of benefit payments under the various adjustment programs, and it is the universal experience that receipt of these payments in a community exerts a pronounced stimulus to trade.

The September 1 crop report showed no material changes, except a drop of 122,000,000 bushels in the indicated corn crop (to 1,485,000,000), which was a little less than expected. The cotton estimate was slightly increased to 9,252,000 bales, though the trade had looked for a decrease. It is probable that any further revision in crop figures this month will be upward, by reason of the rains, but for the chief crops except cotton and late corn, where the frost date is a factor, September 1 estimates are not usually subject to much change. The fact that the crop season is a disaster is now unalterable, but its economic effects are mitigated by the surpluses carried over from the previous year, and by the price advance. The better condition of the pastures and late feed crops this month has cheered the dairymen and live stock feeders, who at best are facing a tight situation.

Farm prices have been slightly easier, but this is evidently more of a reaction from the previous rapid advance than a reflection of change in any market situation. The reaction in hog prices, for example, does not alter the fact that the weight of hogs to be slaughtered in the next twelve months is estimated from 35 to 45 per cent less than in the past twelve, and this situation cannot change short of a year to eighteen months. Choice cattle have continued strong, with the Government purchases, now approaching the goal of 7,500,000 head, kept out of commercial channels. The drop in cotton reflects the textile strike, and the competition of foreign growths, curtailing exports.

Grains on an Import Basis

An effect of the drouth which is of outstanding importance in the general economic situation is the fact that from time to time United States grain prices have risen to a sufficient premium above world prices, at seaboard markets or terminals near the Canadian border, to invite imports of foreign grains over the tariff wall. This has been true of rye for some time; substantial imports of Polish rye have been received, and Canadian rye also has crossed the border. Canadian durum wheat has been imported, and it is understood that a sizable quantity of Canadian Spring wheat has been sold to Northern millers; at any rate the price relationships existing at times would have made such business profitable over the tariff. It is likewise understood that Argentine corn has been booked for shipment to this country. Argentine oats have already been received at Gulf ports for shipment to the interior; and Argentine flaxseed will certainly be wanted to piece out the short crop here. Price relationships also suggest that Canadian barley will move to this country.

This is a striking reversal of the position which the United States has historically occupied as a surplus producer and exporter of the grains. Moreover, we shall be importers of livestock feed and forage from Canada, President Roosevelt in August having authorized their admission free of duty. Exports of cotton are running low, the total from August 1 to September 20 having been but 511,000 bales, compared with 1,064,000 last year and 915,000 two years ago. This drop is not, of course, due to the drouth, but with the other factors cited will be an influence that may considerably alter our trade figures this Fall from what they have been in the past, diminishing the balance in our favor.

A further comment upon the situation, in view of the claims made for the devaluation of the dollar as an influence raising agricultural prices, is that this trade shift clearly shows what the true cause of the price advance has been. The argument ran that the act of cheapening the dollar would make the foreigner's funds worth more in this country, lead to an increase in exports and a mark-up in the prices of all export commodities, and in that manner lift the entire price structure. But the fact is that exports of cotton, the only one of the commodities mentioned selling freely on the world markets, have actually diminished as shown, and there has been an equal or greater price rise in all the grains, of which we are importers rather than exporters. It is plain that exchange rates in either case have had little to do with the price, and that the cause of the advance has been almost wholly the improvement in the statistical position of these commodities, accomplished by natural and artificial curtailment of crops during the past two seasons.

Money and Banking

Money conditions showed no material change during September. Member bank reserves declined from the peak levels reached in August, but continued greatly in excess of legal requirements. For New York City banks alone, the total of this "excess" averaged more than $500,000,000, and for all member banks more than $1,700,000,000.

Money rates remained unaltered at the low levels current for some time. Yields on short-

term Treasury bills, however, continued to work slightly higher, in keeping with the tendency throughout the Government list. In the last week of the month $75,000,000 182-day bills were sold on an average discount basis of 0.29 per cent, compared with 0.22 per cent a month earlier, and 0.07 at the low point in July.

The decline of bank reserves during the month was due principally to a seasonal increase of money in circulation and to a temporary shift of funds from the market to the Reserve Banks in connection with income tax and other transactions for Government account. The rise of money in circulation amounted to about $58,000,000, and was indicative of increased payrolls and more active retail trade after Labor Day.

A feature of the bank statements was the steady rise in loans classified as "all other," which are considered generally indicative of the trend of commercial borrowing. These loans have increased $265,000,000 since July for the weekly reporting banks, the largest gain since last Autumn. The advance is seasonal in part, and accords with the increase of currency in circulation in indicating an expansion of commercial activities.

While "all other" loans advanced during the month, loans on securities declined to new low levels. Investments in Government securities, which declined during August, increased in September. Investments in securities other than Governments rose to the highest point since the bank holiday.

Bond Market and Foreign Exchange

The bond market early in the month continued under the influence of currency and budgetary uncertainties, with Government and corporate bonds extending the declines which had been in progress since July. Later, however, the market became firmer, accompanying a recovery of the dollar in the foreign exchanges and a cessation of gold exports. Prices of the long-term Treasury bonds are now about midway between their January lows and the peak reached in July.

New offerings of State, municipal and corporate securities during the month were small, except for an issue of $75,000,000 of eight-months notes placed by the State of New York with a group of banks on a 7/8 of one per cent basis. New security offerings, exclusive of refunding issues, totaled $1,003,000,000 for the first eight months of the year, according to the Financial Chronicle. This total was larger than that in the corresponding period of either 1933 or 1932. The increase, however, was almost entirely in the issues of States, municipalities and government agencies, corporate financing showing no change and comprising only $128,000,000 of the total.

The reactionary trend prevailing in the bond market during the first part of the month had its counterpart in the foreign exchange market where dollars continued weak in terms of gold currencies. Between September 1 and September 8 gold exports exceeded imports by approximately $17,000,000, following a net excess of exports over imports of $10,000,000 during the last half of August. Around the middle of the month the dollar strengthened on what appeared to be official support, and during the balance of the month remained above the gold export point. Sterling exchange likewise declined further in September, dropping to a new low point of $4.96½ in terms of present day devalued dollars, equivalent to $2.92 in terms of old dollars. On September 3 the price of gold in the London market reached a new high level of 141s.7d. per ounce (equivalent to $35.43). Late in the month European gold currencies turned weak against both dollars and sterling, and in the Far East Japanese yen dropped abruptly from 30 cents, where it had been for over a year, to around 29.20.

Government Conversion Operations

The Government's debt conversion operation has been the outstanding event of the month, both because of the magnitude of the transaction and the importance of any major step affecting Government finances at a time when so much depends upon the maintenance of the public credit. On September 10 the Treasury offered two-year 1½ per cent notes in exchange for the $525,000,000 of certificates maturing on the 15th, and either four-year 2½ per cent notes or 10/12-year 3¼ per cent bonds in exchange for the $1,250,000,000 of Fourth Liberty 4¼s called for payment October 15. As an added inducement to conversion the Treasury offered to pay interest in full on tendered Libertys to October 15.

Holders of maturing certificates were prompt to accept the two-year notes, and on September 17 the Treasury announced that practically the entire issue had been converted. The conversion of called Libertys, on the other hand, has proceeded more slowly. On September 24 when the Treasury closed its books on further subscriptions to the notes, total conversions amounted to $844,000,000, of which $596,000,000 were into the notes and $248,000,000 into the bonds.

With the books still open for conversions into the bonds, it is apparent that the Treasury will have no difficulty in taking care of any unconverted portion on October 15 out of its large balance of cash on hand. This balance has been further increased recently by weekly sales of Treasury bills in excess of maturities, and on September 25 amounted to $2,190,000,000 of which, however, over $800,000,000 repre-

sents part of the "profit" on gold revaluation which Secretary Morgenthau has stated to be under lock and key "for the present."

Terms of Conversion Compared

The maturity and the 3¼ per cent coupon on the new bonds are the same as those carried by the bonds offered last April when a total of $1,037,000,000 was disposed of in exchange for called Libertys and maturing notes. As compared with the June financing, however, the terms are considerably less advantageous to the Government under money conditions practically identical. At that time the Government was able to convert $489,000,000 of maturing certificates and notes into 12/14-year bonds bearing 3 per cent, and in addition to raise $800,000,000 of new money—$300,000,000 through cash subscriptions to the bonds and $500,000,000 through cash subscriptions to five-year 2⅛ per cent bonds. Comparing these terms with those of the current offering, it will be seen that in a purely refunding operation in which no new money is involved the Treasury is paying ¼ of 1 per cent more on its long-term issue, while reducing the maturity by two years, and ⅜ of 1 per cent more on its note issue, while reducing the maturity by one year. In addition, the Treasury is granting a bonus of full interest to October 15 to all who accept conversion.

Notwithstanding these inducements, the conversions into long-term bonds apparently have been considerably smaller than in June. To the extent of course, that holders of Libertys fail to convert into the 10/12-year 3¼s the operation will fall short of one of its primary purposes, which was to reduce the sum total of maturities falling due in 1938, and so improve the debt structure. It is true, of course, that the exchange of called Libertys for notes reduces the burden of interest payments, but such a shift leaves the problem of the debt structure just where it was before, since all that it accomplishes is the replacement of one four-year maturity by another.

In the absence of any change in the money situation, it is evident that the higher cost of the current offering has been due to a more cautious attitude on the part of investors. The silver purchase program instituted during the Summer, continued uncertainty over the future of the dollar, and waning hope of the Government's ability to effect the promised balance of the budget by 1936, have been among the influences that have disturbed the market.

Government Receipts and Expenditures

While Government bonds have been declining, and uneasiness regarding the budgetary outlook increasing, the current position of the Government with respect to receipts and expenditures has shown improvement. For the period from July 1 to September 25, the deficit of $525,000,000 was the smallest for any quarter since a year ago, and much below the deficits incurred during the period of maximum spending in the Winter and Spring. This improvement in the ratio of receipts to expenditures has been due partly to a rise in receipts, but mainly to a decline in expenditures. Receipts amounting to $920,000,000 were 43 per cent larger than in the third quarter a year ago, and larger also than in any intervening quarter. Expenditures, on the other hand, were substantially lower than in preceding quarters, though higher than in the third quarter of last year. The following table, comparing the figures of receipts and expenditures, together with the deficit, by quarters, will show what the trend has been over the past twenty-one months:

Government Receipts and Expenditures
(In Millions of Dollars)

Calendar Year	Quarterly Period	Total Receipts	Total Expenditures*	Deficit*
1933	Jan.-Mch.	$499	$1,117	$ 618
	Apr.-June	558	1,366	808
	July-Sept.	672	909	237
	Oct.-Dec.	797	1,712	915
1934	Jan.-Mch.	837	2,226	1,389
	Apr.-June	810	2,257	1,447
	July-Sept.**	920	1,444	525

*Includes expenditures for statutory debt retirement.
**Through September 25.

Analysis of receipts reveals the principal sources of increase to have been the processing tax on farm products, income taxes, miscellaneous internal revenue and seigniorage. The latter item, which in the past two months has reached $50,000,000, represents the "profit" taken when the Government purchases silver bullion at the market price of around 50 cents an ounce (or 64½ cents for American mined metal) and then transfers it to the monetary silver fund at a valuation of $1.29 an ounce, crediting the mark-up to its "receipts."

Expenditures during the third quarter of this year dropped below those of the preceding quarters mainly because of reduced expenditures by the R.F.C. which during the early part of the year was called upon to make large disbursements in connection with purchases of bank preferred stocks and debentures, and allocations of funds for the use of other Government agencies for relief purposes, including the C.W.A., farm mortgage relief, commodity loans and subscriptions to capital stock of the Home Owners' Loan Corporation. Moreover, expenditures in the third quarter included nothing towards the sinking fund, which, of course, must be made up sometime later during the fiscal year.

As compared with the third quarter a year ago, expenditures of the quarter just closing show an increase of $594,000,000 of which

$517,000,000 comes under the classification of "emergency." The purposes for which these emergency expenditures were made, and the amounts, together with comparative figures for the third quarter of last year, are listed in the table below:

Government Emergency Expenditures, 1933-1934
(In Millions of Dollars)

	July 1 to Sept. 25 1933	1934
Agricultural Adjustment Admin.	$ 9	$ 78
Farm Credit Administration	15	14
Federal Land Banks	6	9
Federal Emergency Relief Admin.	—	361
Civil Works Administration	—	8
Emergency Conservation Work	63	95
Department of Agriculture—Relief	—	20
P.W.A.—Tennessee Valley Authority	—	7
P.W.A.—Loans to railroads	—	46
P.W.A.—Loans, grants to states, etc		33
P.W.A.—Public highways		128
P.W.A.—Boulder Canyon project	63	7
P.W.A.—River and harbor work		45
P.W.A.—Subsistence homesteads		1
P.W.A.—Other		80
Federal Savings & Loan Assns.	—	3
Emergency housing	—	1
Reconstruction Finance Corp.	124	141-C
Admin. for Industrial Recovery	1	3
Total emergency expenditures	$280	$797

C—Excess of credits (deduct).

The table shows the diminished activity of the R.F.C. since a year ago, the increased importance of the P.W.A. as an agency for "priming the pump," and the larger expenditures for direct relief. Since the beginning of the current fiscal year on July 1 the R.F.C.'s payments into the Treasury have exceeded its drafts against the Treasury by $141,000,000 as a result of large repayments by borrowers, decreased demand for new loans and the sale to the public of municipal bonds from its portfolio. The marked expansion of the Home Owners' Loan Corporation and the Federal Farm Mortgage Corporation, whose bonds are guaranteed but are not direct obligations of the Government, has eased the demands upon credit agencies financed wholly from Government funds. Up to August 31 a total of $1,324,000,000 of H.O.L.C. bonds and $625,000,000 of F.F.M.C. bonds had been issued, and the combined direct and indirect debt on that date, including R.F.C. debentures held outside of the Treasury, exceeded $29,000,000,000.

Expansion of Foreign Cotton Growing

We have already referred in passing to the decline in the exports of American cotton this season, and to the increased competition which the American staple is meeting abroad from cotton of foreign growth. This is a subject of which all Americans who come in contact with foreign cotton circles are hearing a great deal, and manifestly it is one of great importance, affecting directly a very large section of this country and indirectly our entire economy. Cotton normally constitutes the largest single item in our export trade, more than half the crop being shipped, and in some years the value of our cotton exports has represented over 20 per cent of total exports. If there is danger that this trade may be permanently curtailed by foreign competition it obviously adds very much to the complexities of the agricultural situation, and places a great responsibility upon the agencies which are determining governmental policies with respect to cotton.

It was recently stated by a Government authority that more than fifty foreign countries were growing cotton. As a matter of fact a study made by the International Institute of Agriculture in 1926 listed seventy-four countries growing the crop in some degree, and while in the majority of them the quantities produced are insignificant and the areas incapable of much expansion it is evident that there are a number ready to grasp at the scepter of King Cotton if the United States should elect to lay it down.

The present interest in the situation arises from the fact that while production of American cotton has been curtailed for three consecutive years the production of foreign growths has advanced very rapidly, as shown by the following table from the New York Cotton Exchange Service:

Cotton Production (Thousands of bales)
American cotton in running bales;
foreign in equivalent 500-lb. bales

	1924-25 1928-29 Average	1931-32	1932-33	1933-34	1934-35 (preliminary) estimates
American	15,172	16,877	12,961	12,715	9,142
Foreign	10,322	9,858	10,624	12,646	13,225
Total	25,494	26,535	23,585	25,361	22,367
Per cent American	59.5	63.6	55.0	50.1	40.9

The 1934-35 figures are tentative and according to some other reports may prove high. Even so, the figures reveal an extraordinary reversal, within three years, in the proportions of American and foreign cottons in the world crops. Clearly the shift to the use of foreign cottons will be very much greater this season than last. Prices of Indian and other cottons abroad are substantially below their normal relationship to American, and spinners naturally substitute them as much as considerations of character and quality permit.

It is important to understand that the shift shown by the figures is in no way accidental, but is the natural and inevitable response of foreign growers to changing economic factors. It is due not to better than average growing conditions, except in small degree, but to increases in foreign acreages, and the basic reason for the acreage increases is that cotton has become relatively more profitable than other crops, especially since the price advance began a year and a half ago. This traces the main cause back to the United States, for it is admittedly the policy of crop destruction and restriction followed here which has raised the price.

History of Foreign Competition

American cotton growers have always been rather complacent toward foreign competition. At times in the past they have been aroused by some especially marked increase in foreign yields lasting over two or three seasons, stimulated by short crops and high prices for American, but the outcome has always been that a return to larger crops and lower prices here has slowed up other growths again, and the "menace" has passed over. During our Civil War there was a rapid expansion of foreign cotton growing. The Egyptian and Indian crops rose from around 100,000 and 600,000 bales, respectively, before the War, to above 500,000 and 2,000,000 in 1865. Subsequently, however, there was a slump. Egypt recovered earliest, and equalled the 1865 crop in 1873, but the Indian crop was not again as large, with one exception, for twenty-one years. Brazil under the War influence became a cotton producer of some importance, exporting to Great Britain in 1868 637,000 bales (of around 200 lbs. each). Thereafter, although she made a valiant effort to hold her position against reviving American production, she lost ground steadily, until in the low price era of the '90s her cotton export trade almost disappeared.

The most recent experience, familiar to everyone, was the expansion abroad which followed the short American crops of 1921, 1922 and 1923. These led to prices as high as 37 cents in the latter year, and soon thereafter the increase in foreign growths became the leading topic in the trade as it is today. From 6,880,000 bales in 1921-22 foreign crops rose to 10,399,000 in 1925-26. However, the larger American crops after 1923 and the price decline culminating in the Fall of 1926 slowed down the expansion, and after a brief gain in 1928 and 1929 the total of foreign growths once more fell below 10,000,000 bales in 1931-32.

Based upon these historical experiences with spurts that were not sustained, and certain of the natural advantages of the American cotton belt over other areas and the superior quality of the staple, American growers have felt secure in their supremacy. But there is an obvious difference between the present and past situations, for while the short American crops of the past were natural calamities and were naturally followed by compensating larger crops, those of the present are arbitrarily restricted and the policies that will follow the restriction are still subjects of uncertainty. If the limitations are to be continued no reliance can be placed on these precedents.

Old and New Cotton Areas

In some foreign countries such as India, China and Egypt cotton production is well established as part of the agricultural program, and in these countries considerable variation takes place from year to year in response to changing economic conditions, just as in the United States. In short, they are prompt to expand, but equally prompt to curtail, and will do so if American crops increase again and prices decline. Moreover, the acreage planted in these countries in a favorable year such as this one is likely to represent almost the practicable maximum.

In Egypt within the past five years the cotton area has fluctuated between 2,160,000 acres (in 1930) and 1,135,000 (in 1932), and the former is about the limit that can be given to cotton after planting necessary food and feed crops. The preliminary estimate this year is 1,798,000. Any increase over 2,160,000 would require extensive and costly irrigation and drainage systems to reclaim waste lands, and the capital expenditure is unlikely.

In India, with its 300,000,000 population, food crops are of first importance. The peak of Indian cotton acreage came in 1925-26, and it is not expected to be equalled even this year. In China the increase in the past two years has been impressive, from 1,106,000 bales in 1931-32 to well over 2,000,000 estimated for the current season. However, the requirements of food production limit the cotton acreage, and the area where cotton growing might be expanded lacks adequate transportation, which is a double handicap in that it makes both the export of cotton and the import of food an expensive process. Hence food comes first.

Russia is both an old and a new cotton country. The expansion in acreage which took place a few years ago brought most of the land now available for cotton into the production of that crop. Developments on new lands are being promoted, but the physical handicaps, including high transportation costs and need for irrigation, are heavy, and current reports are rather unfavorable. It is the opinion of both the Department of Agriculture and private experts that Russia has reached her practical maximum, pending large capital expenditures and establishment of better growing practices. Moreover, her consumption is certain to expand as rapidly as her production, in view of the needs of the people, and her crop does not figure in world markets.

All the countries mentioned can be expected to push their cotton production to a maximum when American cotton is scarce and high, and conversely to curtail when American is abundant and cheap, or other crops relatively higher. There are in addition certain new or potential areas where the stimulus given to cotton growing during periods such as these may result in permanent gains in production. In these countries the development of cotton growing is frequently in the hands of the Gov-

ernment, or private promotional associations and development corporations play the principal role. Large capital expenditures have been made, and agricultural programs are less flexible. Hence production gains are likely to be held, or approximately so, even when the other countries are contracting. In the main, however, these countries are small and all their crops put together a minor factor.

Continuous efforts have been made to develop cotton growing in new countries within the British Empire by the Governments concerned and by the British Cotton Growing Association, an organization supported by Lancashire spinners. Production in these new fields (Africa, Australia and certain islands) expanded from 100,000 bales (of 400 lbs. each) in 1922 to 440,000 in 1926. Further growth has been slow, the 1933 total having been 518,-800. Lord Derby, President of the Association, stated at the annual meeting last May, that "with any luck at all" these countries could produce 1,000,000 bales. This is a creditable performance, but the figure is small as compared with our production. The highest hopes entertained have been for the Sudan, but a recent analysis of the Sudan situation made by P. K. Norris of the U. S. Department of Agriculture appears to be chiefly a recital of difficulties. It notes that the financial returns from the irrigation projects have fallen far short of estimates (to be sure the depression has intervened), that various production problems have not been solved, and that in no year has the crop exceeded 10 per cent of the early estimates of its potentialities.

Cotton production in Asia Minor, Mexico, Peru and other countries has been expanded since the War, and the acreage where reports are available generally shows increases this year, though the crops may not be larger in all cases. Manchuria is engaged in cotton growing, with 198,000 acres in production this season.

In all these countries the possibilities are quite limited, but cotton, an exportable cash crop, is valuable to their national economy, and the situation is helping business conditions.

Brazil May Become Large Producer

We have reserved for a fuller description the country which has had the most rapid growth of all in the past two years and has the greatest possibilities of future expansion, which is Brazil. The late Arno S. Pearse, for many years secretary of the International Federation of Master Cotton Spinners and Manufacturers Associations, devoted much time to personal surveys of cotton-growing possibilities in various countries, and published several books on the subject, and Brazil was the one country which engaged his enthusiasm. He states in his book "Brazilian Cotton" (1921) that no other crop is more suited to Brazil, that the yields are "phenomenal," and that "cotton is bound to assert itself." He pointed out at that time that "what Brazil has produced, and excellent qualities are grown, has been achieved without the least human effort toward improvement. All is the spontaneous work of bountiful natural conditions."

At that time Brazil was producing around 400,000 bales (478 lbs.) annually. This increased to 660,000 in 1924-25, thence dropped below 400,000. But in the current year the combined total of the Southern crop harvested from May to July, and the Northern crop harvested from August to January, is officially estimated at the equivalent of 1,250,000 American bales. Moreover, private reports from Sao Paulo suggest that the next Southern crop may be increased by 50 per cent or more over this year's figure of 500,000, if the labor is available.

This is entitled to be called a boom, verifying Mr. Pearse's 1921 estimate of the possibilities. He made a great point at that time of the handicaps due to inferior ginning, picking, classing and handling, and the lack of uniformity of fiber caused by mixing seed. There is evidence, however, that under the leaders who have developed the cotton-growing industry since that time conditions have been improved to a point which satisfies Manchester spinners. Brazilian cotton has a good name for quality, comparable with American. It is of better staple than most of the chief foreign crops, and is sold against American standards.

The extent to which Brazil could conceivably raise her cotton production, if conditions should continue highly favorable over a period of years, is undoubtedly much greater than any other country. Her land area suitable for cotton is larger than that of the United States, and her yields are higher. Of course she is relatively deficient in transportation and handling facilities, and the labor supply is by no means adequate to support a continuous rapid expansion. The speed of the present growth is due to the greater profits to be obtained in cotton at present prices compared with coffee, and any reverse change in this relationship would doubtless check cotton growing. However, it is not to be overlooked that development work has now been done and capital invested in the industry, and as costs of production are believed to be lower than in the United States it is probable that Brazil will continue to grow cotton for export on a substantial scale, even under conditions less favorable than now exist.

Decision in American Policies Necessary

The history of foreign cotton crops has shown that there is a natural upward trend in them due to the extension of production in new areas, and that this trend is speeded up or

retarded as American crops are small or large. Ordinarily the expansion would not be rapid enough to exceed the normal growth of consumption, and hence would not reduce permanently the share of the United States in the world cotton markets. The foregoing figures give a plain indication, however, that the policy of restricting production and raising prices in this country, even though it leaves available a more than ample supply of American cotton, leads to expansion of competitive growths, restricts the consumption of American, and so perpetuates the surplus problem. It induces the old countries where cotton is long established to grow it to their full capacity, and if continued long enough it may induce capital expenditures which will increase their capacity. It stimulates rapid expansion wherever practicable, as in Brazil, and after cotton growing is well established nothing short of another economic debacle is likely to drive it out again.

The experience will be recalled of the British rubber producers. Prior to the Stevenson plan they had as large a share of the world rubber market as this country has of the world cotton market. As a result of that plan they lost part of their market to the Dutch, while the surplus problem still persists. The experience of the Cuban sugar producers and their effort in 1926 and thereafter to hold up the sugar market through crop restriction, and the lesson of the stimulation given to the mild coffee crops, prior to the depression, by Brazil's coffee valorization scheme, also illuminate the cotton situation.

On the other hand, it has been demonstrated in the past that competition with American cotton is not permanently effective, and expansion is quickly checked, if the American grower is free to respond to the same price influences which affect foreign growers, and to increase his own crops.

Evidently a decision as to policy in the cotton program of this country is called for. Mr. Tugwell, the Under-Secretary of Agriculture, has stated that "the time is at hand when the temporary and emergency program must be transformed into something of a permanent policy." He recognizes that "the people of the South abhor the thought of ever surrendering dominance in the world's markets," but adds "I doubt if you will care to enter into world competition again for six-cent cotton."

If American producers seek to obtain a price above what other countries are willing to grow cotton for they must expect to sell less, and many of them will have to give up cotton growing for other occupations. The violent economic adjustments that would be necessary as the result of permanent wholesale restriction of the cotton crop are scarcely to be contemplated. If on the other hand American producers elect to compete in world markets they have great natural advantages to enable them to do so.

It is stated that it is the standard of living of the cotton growers which is really at stake, that for reasons of national welfare they should not attempt to compete with foreign cotton produced under living conditions lower than the very worst in this country. With all respect, the way to improve the growers' standards of living is to increase the efficiency of their operations, as the agricultural departments and colleges are doing, so that they may produce more cotton on fewer acres, and at lower costs. There is a basic contradiction in the allegation that the standard of living in the country with the greatest natural advantages is determined by other countries less favored. We lack space to go fully into the economic factors which control the cotton farmers' living standards, but it is safe to say that they are largely in the field of domestic cost and price relationships, and agricultural practices, and hence are internal rather than external factors.

Plans for Creating Purchasing Power

There is common agreement that the state of depression and unemployment indicates a lack of purchasing power in the hands of the people, and a great many plans have been proposed for overcoming this condition. The latest, said to have originated in California, but to be spreading rapidly eastward, is to establish Federal pensions of $200 per month for all persons who have reached the age of sixty, with provision that the recipients shall spend the full stipend each month. That this scheme responds to a long felt want is evident not only from the enthusiasm which it is said to inspire, but from the number of proposals which embody the idea that Treasury expenditures for the support of the indigent not only serve that purpose but are of themselves a new source of purchasing power and a wellspring of general prosperity.

It is important to distinguish between the two considerations. Throughout civilized society there is practically no dissent to the sentiment that the weak, unfortunate and helpless members of the community shall be provided with the common necessaries of life at the public expense. This is a tribute which humanity owes to its own kind, in the name of its common origin. How liberal such a policy of support should be is not at this point an issue. The point here is that such outlays always have been recognized as expenses, borne by the rest of the community and diminishing its ability to use purchasing power for other purposes.

A proposal to establish old-age pensions also is one which has standing as a question of

public policy, and we need not enter into a discussion of it in detail. A number of nations have such systems, but everywhere they are recognized as an expense item in the budget, to be covered by taxation. The argument for them has been that the aged have borne in their time a useful part in upbuilding the national wealth, and that the national income is sufficient to bear the award of this additional compensation when their earning powers have declined. The idea that pensions may be a source of new national wealth has not been a factor in them.

Evidently it is a very important innovation. If accepted as a sound principle it provides a most persuasive appeal for every proposal to appropriate Treasury funds or use the Government credit. Indeed, if it is true, the individual merits of any proposal become of only comparative importance, since all have this element of good, even possibly, to the satirical suggestion attributed to Governor Talmage of Georgia, that money in bundles be scattered from airplanes. However, we have many old adages which have been passed down to us as embodying the common sense conclusions of mankind and which have bearing on this idea: Such as "Save for the rainy day," "You cannot eat your cake and have it too," "You cannot have it both ways," "You cannot lift yourself over the fence by your bootstraps," etc. These warnings imply that always there have been people who did not keep their feet on the ground. The adages are in accord with the commonly accepted principle that since the Government obtains its own support from the people, it is irrational to suppose that it has resources for supporting the people.

This may be said to be evasive comment, since the Government has power to extract from the portion of the people possessing wealth and income the sums proposed for distribution to others. The rejoinder, however, shifts the argument away from the assumption that new purchasing power will be created, back to an agreement that Government expenditures can be properly made only as the Government obtains funds from the public. We insist that it is of the utmost importance to separate the two motives for expenditures and distinguish between them, for they are constantly intermingled in the public mind. The final answer to all the questions involved must come from an understanding of the origin of wealth and purchasing power, the means by which they are normally distributed, and the confusion which must result from efforts of the Government to accomplish an enforced distribution.

The Decline of Purchasing Power

So much has appeared in these columns about the disruption of price relations resulting from the war, that we need not give much space to it here. Briefly summarized, the story is that the war gave an abnormal stimulus to production, wages and prices, which induced the creation of a great body of indebtedness, and that after the post-war peace-boom had exhausted itself the war-time and boom-time prices could not be maintained, but declined very unevenly. The Secretary of Agriculture has told how the war demands by Western Europe for farm products stimulated a great increase of production outside of Europe, and that recently Europe has practically excluded our farm products from her markets. This change of trade relations has led him to apprehend that 40,000,000 to 50,000,000 acres of farm lands must be retired from cultivation, which if true means a grave unsettlement of this basic industry.

Table 9 of Senate Document No. 124, as reproduced in our August number shows that the income of Agriculture in 1932 was less than 30% of that of 1929. The same table shows that the income of the construction industry was less than 15% of that of 1929. Construction work was held back during the war, except as devoted to war purposes, with the result that it was abnormally stimulated at the end of the war, at excessive costs and subject to excessive indebtedness. This war stimulus and resulting speculation and use of credit permeated the entire economic system.

In the Appalachian Coal case decided in the Supreme Court last year, Chief Justice Hughes, in rendering judgment, reviewing the state of the bituminous coal industry, said:

> The findings of the District Court, upon abundant evidence, leave no room for doubt as to the economic condition of the coal industry. That condition, as the District Court states, "for many years has been indeed deplorable." Due largely to the expansion under the stimulus of the Great War, "the bituminous mines of the country have a developed capacity exceeding 700,000,000 tons" to meet a demand "of less than 500,000,000 tons."

The board of mediation in the textile industry recently appointed by President Roosevelt in its lengthy report to him, describing the troubles of the industry made the following reference to the effects of the war upon it:

> During the war the industry expanded enormously in order to meet unusual war conditions. Mills which had formerly been operated on a one-shift basis began to run two shifts or more. After the war, demand fell off and the industry found itself overexpanded. Even during the boom years before 1930 the cotton textile industry as a whole was not considered prosperous.

Obviously the difficulties of every industry reacted upon all the others with cumulative effects.

The Monetary Remedy

All of the foregoing has bearing upon one of the most strenuously urged plans for creating purchasing power, viz: by inflating the currency. It is based upon the theory that there is scarcity of money with which to transact business, although at no time since 1929 has the stock of money been less than in that

year. The plan disregards the obvious truth that commodities and services are purchasing power in themselves and that more than 90% of the trade of the country settles itself in the busiest times without the use of money; also disregards the evident disruption of trade relations between the several sections of the productive system, which fully accounts for the appearance of surpluses, and the fall of prices, loss of purchasing power and increase of unemployment.

Moreover, the injection of more money or Government credit into such a situation on a large scale introduces a new unbalancing influence. The basic principle of the economic system is the exchange of services. The trade of the country, left to itself, practically settles itself daily through more than 400 clearing houses. Each section ships out its own products and receives practically corresponding values from the rest of the country or world. If now the Government enters the construction field with great expenditures for projects which are prompted largely by the motive to provide employment, and from which any other possible return must be delayed for many years, where is the compensating flow to the body of taxpayers who must currently pay the cost, or if that is covered by loans keep up the interest payments? The national economy must balance, as it normally does, in the exchanges between the different groups and sections of the industrial system, but to take capital from the body of the people by taxation or loans for investment in works which will produce no income in the near future must tend to aggravate rather than remedy the disorders of an unbalanced economy.

There is a tendency to think of these expenditures of capital upon construction work as though they were of the same continuing and self supporting character as the regular exchanges which settle themselves as they go along and may go on perpetually. This discussion is about emergency expenditures, prompted by other purposes than those of ordinary business investment, and from which no early returns are probable. It is evident that the temporary stimulus given to general business by the disbursement of capital funds would not compensate for sinking the funds permanently, with no expectation of return; and so it is a fair question in each case, whether the prospect of a return justifies the taxation or borrowing which supplies the funds. The emergency investments cannot go on indefinitely without producing returns and the direct stimulus of disbursements will cease when they cease.

An Example of Public Works

In order to make clear the meaning it is always desirable to reduce general statements to concrete terms and to illustrate the foregoing the appropriation to improve the Missouri river from Kansas City to Sioux City for navigation, may be named as an example, and that project may be compared with the reconstruction of the Erie canal by the State of New York about twenty-five years ago at a cost of approximately $230,000,000. The possibilities of the Erie canal for business would seem to compare quite favorably with those of the Missouri river project. It has twelve feet of water at all times, which probably is twice as much as by any possibility can be assured to the river, and it is located in a populous region, passes through numerous important cities and is on the main line of traffic between the Middle West, the Great Lakes and the Seaboard. The canal is maintained and the fixed services operated by the State free of tolls upon traffic, but it is credibly stated that the State could well afford to ship by rail at its own expense all of the freight which passes through the canal, if by doing so it could be relieved of the operating and upkeep costs, saying nothing of a return on the investment. Would anybody maintain that the benefits derived from the construction expenditures have compensated the State for its investment up to this time or that a multiplication of such investments would make for prosperity? Incidentally it may be mentioned that the Missouri river appropriation contains a provision that the minimum wage for common labor employed on the project shall be 45 cents per hour and of skilled labor $1.10 per hour, the purpose being to set a standard for private business. This illustrates the combination of motives avowedly prompting such appropriations.

The above statement of the original cost of the reconstruction and improvement of the Erie canal would not have its full significance if we did not add that a total of $163,800,000 of bonds were sold for the work, of which approximately $151,000,000 are still outstanding. Inasmuch as the rate of interest has averaged about 4%, the interest payments have about doubled the State's investment in the reconstruction enterprise.

There is a socialistic slogan that "production should be for use and not for profit," but if "use" is defined to include disbursement without the prospect of a return which can be used elsewhere,—in other words of a return which will reproduce the value sunk—all of the available capital of the country might be tied up in such enterprises, after which "production" and "use" of that kind would certainly come to an end. The theory would have run itself into the ground. The rule that capital should be invested with some regard for prospective results is necessary to keep the limited capital fund from being wasted. Furthermore, common sense would seem to dictate that projects which promise the largest usefulness

should be selected first, which is simply the test of private enterprise and the means by which economic development is kept in balance.

The Use of Credit Currency

There is a tendency to theorize in a vague way that somehow the Government, by means of its credit and sovereign power can maintain the equilibrium which would be disturbed by the diversion of private capital into long-term investments promising no early returns. But as said above, the use of such powers would be another disturbing influence. If expenditures of the class under discussion were financed by the creation of Reserve credit or legal tender currency, consideration would have to be given to the danger that the monetary system would be unsettled, and that even apprehensions of such developments might have serious effects.

The problem is one of dealing with realities, for the Government is only the agent of the people. Its undertakings are their undertakings and debts can be liquidated only by the creation of values.

Credit is the economic term for Faith, and Faith has been forever defined as "the substance of things hoped for, the evidence of things not seen"; but the credit under contemplation here is a mortgage on future prosperity, which will not be good security until we have learned how to create the reality.

The Country's Tax-Paying Capacity

If the theory that disbursements to the indigent and unproductive members of society constitute a new stream of purchasing power flowing into the channels of trade is discarded as visionary, and it is agreed that large expenditures financed by Reserve credit or legal tender issues would be imprudent, then there remains the question of how far the Government can safely go with the policy of transferring wealth from the portion of the community which possesses it to the support of those who are in need. Undoubtedly the opinion prevails that there are vast holdings of surplus wealth which may be so converted. The first comment to be made upon this belief is that the great body of existing wealth is in the form of fixed property, such as farms, business blocks, warehouses, residences, factories, industrial equipment, etc., etc. Such property cannot be distributed or sold for distribution for the purpose in view. Much of it is already mortgaged and real estate mortgages are not in high favor at present. About the only practicable collection of taxes in times like these is out of current income, and that must be mentioned with reserve.

In the August issue of this Letter we gave the figures for the distribution of the total national income in the four years 1929-1932, and last month we gave profits of all corporations over a term of years, and refer the reader thereto. These figures show that in the years 1930, 1931 and 1932 the proprietors of business in the aggregate suffered heavy losses of working capital. Official figures for 1933 are not yet available. Although some recovery occurred in that year, the net earnings certainly were much below normal. We have already mentioned that the capital in fixed investments cannot be converted for distribution either for tax-payments or operating expenses. The losses fall upon working capital, which is only a margin of the whole, and none too large a margin to finance a recovery of prosperity. These losses in the three years named aggregated about *Ten Billion Dollars,* not including unearned dividends paid to shareholders, which were maintained through reluctance to discontinue them, but which represent a loss to working capital.

The Business Organization plans and directs all of the economic activities, provides the employment, the income, the daily production and distribution of the necessaries of life to all of the people. This Organization has developed through all of the past, and anything like a general breakdown and suspension of its activities would mean anarchy. Wage-earners are as much dependent upon it as stockholders. It is not in the interest of the wage-working class that the working capital of the industries shall be dissipated in losses year after year. Every bankruptcy and suspension of operations means more workers out of employment. The entire program of unemployment relief, whatever it may be, and of support for all the activities of the Governments, national, state, and local, depends upon the maintenance of the Business Organization. A large proportion of the industrial companies have had losses year after year since 1930 and are seriously weakened by them.

In 1929 the total value of all goods and services entering trade in this country was $83,032,000,000, and 48,830,000 persons were "gainfully employed," to use the language of the Census. Hence if the total national income had been divided equally among the "gainfully employed" the amount for each one would have been about $1,700, which is less than the amount commonly named as required to provide a decent living for the average family. This would be without any provision for new capital to carry on the improvement and development of the industries, by which the standard of living in this country has been raised to the highest level in the world.

Furthermore, this average of $1,700 was accomplished by the Business Organization, including, as it does, the army of specialists in all lines of efforts, working together to the common purpose. It is an intricate, highly in-

terdependent organization, which rapidly loses its efficiency if thrown into confusion. What would be the result of a continuing increase of the present disorganization. Some idea can be formed from the drop of aggregate income in the period 1929 to 1932 from $83,000,000,000 to $39,365,000,000. Something of the effect upon wage-workers may be judged by the fall in the total of wages and salaries from $52,793,000,000 in 1929 to $31,533,000,000 in 1932. These results were caused by disorganization in the system, a partial blockade of the exchanges, although in the main the producing companies were able to carry on. Surely the preservation of the organization from further disintegration is a matter of vital importance.

We commend a careful study of income distribution and of corporation earnings to any one who assumes that great sums of surplus income may be easily extracted from a comparatively small group of tax-payers to finance the class of investments under discussion.

This article is about "Plans for Creating Purchasing Power," and we are discussing the confusion of the philanthropic or altruistic motive with economic principles, without any purpose to depreciate the former, which is entitled to full consideration in its place. The point simply is that a great deal more money will be available for philanthropy if business is conducted on sound economic principles. Everyone will agree that the best relief for the unemployed is employment, and any one who will read the profit figures of the industries even in the prosperous years 1923 to 1929 can see that if their expenses had been materially higher nothing would have been available for philanthropy and that if the conditions of the last four years should continue, the system would be on the way to ruin.

The Lesson of the Last Five Years

The general policy of the industries since 1929, as influenced by governmental policy and public opinion, and as deliberately adopted by managements, has been that of attempting to maintain wages and prices against downward economic pressure, always on the theory that the war-time and boom-time conditions were a new norm which should be maintained. As a matter of fact they were not maintained and it seems to be rational to carefully inquire why. Nobody can afford to be dogmatic in his opinions; everybody wants to see the country rise out of the depression, and most intelligent people believe that when conditions are right the country will enter upon a period of better, sounder and more abundant prosperity than that of the period 1915-1929 or any other period of the past.

Reviewing the period since 1914, and for the moment leaving money, wages and prices in the background, it seems to be apparent that the changes in physical production and trade have been the master influence in all the other changes. Violent changes in wages and prices have been primarily caused by violent fluctuations in the demands on the industries, thus reflecting the influence of the law of supply and demand. (Incidentally it seems foolish to talk about having a monetary system or system of prices which would not reflect the influence of supply and demand.) The brief reference above to a few of the leading industries indicates the tremendous pressure that all production and business were under during the war. When the war and boom periods were over the pressure relaxed, and prices began to give way. All sentiment and all business were opposed to the tendency and even today this sentiment and opinion are strongly affirmed.

Recently a gentleman very highly regarded in the business world, and who has been actively concerned in the formulation of codes under the National Recovery Administration, delivered a carefully prepared address to an Association of retail merchants in the northwest, in which he set forth this view with the utmost sincerity and fervor. We quote briefly from his description of the collapse of prices in the cotton goods industry:

> In December 1929 within 60 days after the stock market broke badly in October a small manufacturer near Philadelphia, with less than 200 employees, producing a semi-finished product cut wages 15% to obtain business to maintain sales to offset cancellations of orders.
>
> That concern had started within two years on a limited capital and was in competition with a large mill where the proprietor had been employed. That 15% wage reduction and the subsequent cut in the price of the products sold by that mill broke the entire price structure on total sales of hundreds of millions of dollars of one of the oldest established industries in the United States.
>
> It was followed within ten days by a competitor in Rhode Island, then by several others in New England and quickly spread throughout every division of that industry, which in turn compelled every self-contained mill performing all of the processes from the raw material to the product ready for consumption to cut wages to meet the competitive prices of those buying the semi-finished materials from the competitors of that mill which made the original wage cut.
>
> And, of course, that started the stampede.

While this description no doubt is accurate as far as it goes, does it completely account for the fall of prices and unemployment since the depression began? Is it possible to ignore the conditions in agriculture as described by Secretary Wallace, the conditions in the coal industry referred to by Chief Justice Hughes, the conditions in the textile industry described by the Textile Mediation Board, the conditions in the construction industry, in the securities markets, the credit situation, and other conditions affecting the purchasing power of tens of millions of consumers, and assume that but for the price cuts inaugurated by a small manufacturer near Philadelphia prices and employ-

ment in the textile industries would have remained unchanged? Accepting the explanation of Secretary Wallace that the troubles of agriculture originated in Europe, is it allowable to assume that the heavy loss of income suffered by the farm population, and as related thereto, the loss of income by all of the 44% of the country's population living in the country and in towns of less than 2,500 inhabitants, would not affect employment in all the urban industries, and that increasing unemployment in all the other industries would not affect the textile industries?

Senate Document 124, Seventy-third Congress, shows that aggregate wage and salary payments fell off a little more than 40% from 1929 to 1932, which indicates that unemployment, not rate-reductions, was the principal factor in the decline of aggregate payments. Furthermore, in some industries in which wage-rate reductions were small the falling off in employment was very large; thus there have been no wage-rate reductions in the anthracite coal industry, and at no time more than a 10% reduction in railroad wage-rates, but in the first four months of 1933 employment in the former industry averaged 54.4% of the 1929 level and on the railroads 56.5%.

Thus a review of all the conditions seems to show that the loss of business, employment and wages in the cotton goods industry was not so much the result of wage-cutting or price-cutting within the industry as of loss of purchasing power among its customers, and if this is so, does it teach the lesson implied in the above quotation or a different lesson? The loss of purchasing power among its customers resulted not only from the fact that their incomes had declined, but from the fact that what they had to buy, including cotton goods, did not at first decline in like proportion; in short, *from the disruption of price relations.* Having regard for the recognized principle that the entire industrial system is based upon the exchange of services, this seems to imply that the cotton goods industry was directly interested on its own account in maintaining its exchanges on a normal basis, and the tendency of the law of supply and demand was to force readjustments to that end. The question is whether opposition to this tendency was helpful or otherwise to the cotton goods industry and the workers dependent upon it? Incidentally the fact should be considered that the decline of farm products was substantially reducing the cost of living and that a decline of cotton goods would have a like effect.

The Policy of N. R. A.

The policy of the Recovery Administration has been that of raising wages and spreading employment, the purpose being to increase the purchasing power of the wage-earners. The prospective rise in costs and prices stimulated an outburst of buying and of industrial activity last year, but it also caused a rise of prices to consumers which inevitably decreases consumer purchasing power. It was difficult for some observers to understand how any increase in the aggregate of purchasing power could result, for the economic system has no income from outside of itself, and all costs must be charged against consumers; however, that was and remains a controversial question, and we wish now to simply review the experiment as reported by the authorities themselves.

The code for the textile industries went into effect in July, 1933, and the Textile Mediation Board in its report to the President, dated September 20, 1934, describes the conditions relative to wages and working hours established under it as follows:

> It is proper at this time to point out that the cooperation of the industry in promptly adopting the code brought marked improvements in the conditions of the industry. Child labor was, for the first time, completely eliminated from the industry; hours were reduced from an average of fifty-three per week to a maximum of forty; wage rates raised from pre-code levels of $8 or $10 per week to a minimum of $12 and $13 per week; average earnings increased during the first months of the code by 70 per cent; payrolls and employment in the industry rose rapidly.
>
> For the first few months under the code employers and employes alike found their situation substantially improved. Partly due to speculative increases in production during May, June and July of 1933, and partly due to certain aspects of the recovery program, business conditions were better than in years.
>
> In the second half of 1933, however, the industry suffered a reaction and business declined through the remainder of the year. In December the Code Authority made application for and was granted a 25 per cent curtailment in machine-hour operations for that month. There was no public hearing on the curtailment order. No increase in wage rates was made to offset the decrease in working hours.
>
> In the beginning of 1934 there was another upward surge in the industry. Since then business has steadily declined. In May, 1934, the Code Authority, finding that inventories were piling up on the industry, requested a curtailment of machine hours for three months of 25 per cent. This curtailment was granted by NRA for the months of June, July and August, 1934. No public hearing was held on the curtailment order. As will be developed later, it was this curtailment of 25 per cent without an increase in wage rates which caused disappointment among the workers and helped to precipitate the present controversy.

Evidently some consideration was given to the possibility that increasing costs and prices might affect consumption unfavorably, for the following paragraph in the above mentioned report quotes from the code as follows:

> It was stipulated that approval of the minimum wages proposed in the code was "not to be regarded as approval of their economic sufficiency but is granted in the belief that in view of the large increase in wage payments provided by the code, any higher minima at this time might react to reduce consumption and employment, and on the understanding that if and as conditions improve the subject may be reopened with a view to increasing them."

The representatives of both employers and employes who participated in making this code seem to have been agreed that if the code policy should have the effect of reducing the consumption of cotton goods, it would be harmful to all parties concerned.

Mr. George A. Sloan, Chairman of the Cotton Textile Code Authority and also of the Cotton Textile Institute, who by reason of his relation to the industry was active in the preparation of the cotton textile code has given further particulars as to the effects of the code upon employment and earnings, as follows:

The code's most important effect was to spread employment, caused by the reduction of the work week from an average of fifty-four hours to a maximum of forty hours. As a result, the industry was able to maintain a level of employment during the first ten months of operation under the code of 120,000 employes in excess of those employed in March, 1933. In fact, at some periods the increase over March, 1933, reached as high as 140,000 persons.

Even during the present period of slack demand for cotton goods the number of persons at work in cotton mills still stands at 100,000 above March, 1933.

In applying the wage provisions of the code, mills increased the average hourly wage 70 per cent. The result of the great influx of new workers in cotton mills, plus the higher wages, caused an increase in the industry's payrolls during the first ten months under the code, as compared with the ten months prior to the code, of 113,000,000, or 78 per cent. This expansion is of the highest significance as demonstrating the immense increase in purchasing power that became available in mill communities.

Furthermore, it was separate and distinct from any increase in the cotton mill business, as *the volume of production was only 3 per cent greater.* The weekly income of cotton mill workers, notwithstanding the much shorter work week, averaged 6 per cent above 1929, when adjusted to changes in the cost of living.

Mr. Sloan's statement as to the effects of the Code upon employe earnings and employment was confirmed by General Hugh Johnson in a public statement. The most important facts brought out by the two statements are the showing of increased employment and costs accompanying an increase of 3% in production. The reduction of the work-week from an average of 53 or 54 hours to 40 was for the purpose of taking up the slack in employment, but in December, 1933, a curtailment of 25% in machine-hour production was ordered to check the accumulation of goods, and in May, 1934, a curtailment of three months was granted. The textile union then asked for a further curtailment of the work-week and an increase of hourly wages to maintain the weekly wage. This was not granted and eventually the demand was raised to a reduction of the work-week to 30 hours, with the same earnings that had been allowed for 40 hours, and upon this issue the strike was called.

The strike has been called off upon the action of President Roosevelt, proposing to appoint a Textile Labor Relations Board, to have general authority over the industry, for the administration of section 7(a) of the Recovery Act and the code of fair competition in force under the Act, and also for separate studies of matters in controversy. This Board of three members, consisting of Judge Walter P. Stacy of North Carolina, Chairman, James A. Mullenbach of Illinois, and Admiral Henry A. Wiley, retired, of Alabama, has been appointed.

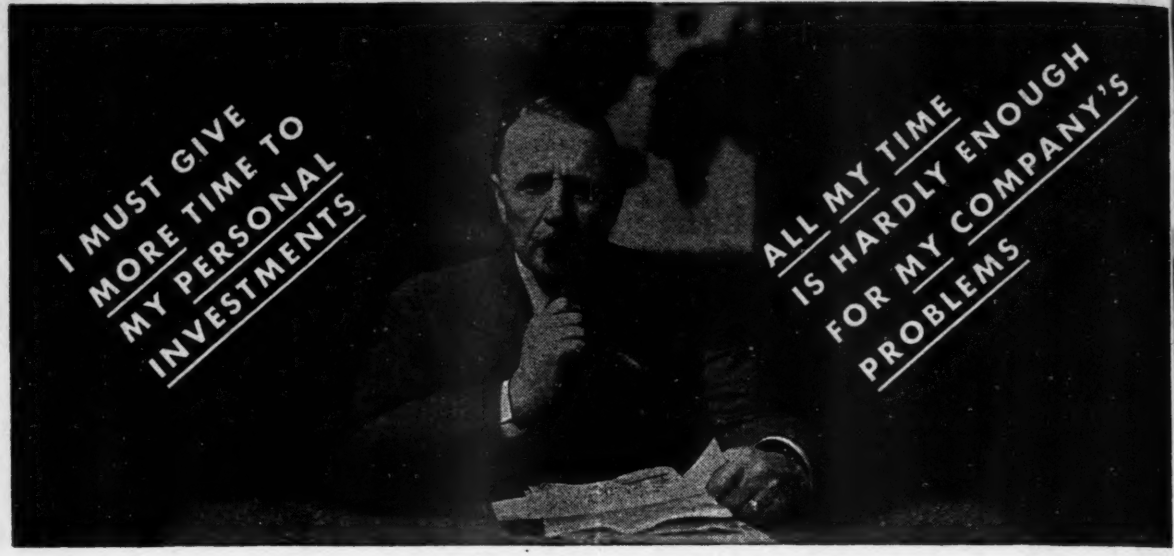
The same executive order provides that the Bureau of Labor Statistics "shall prepare a comprehensive report on the actual hours of employment, earnings and working conditions in the textile industries" and that the Federal Trade Commission shall undertake an investigation "in order to furnish a basis for determining whether wage increases based upon reduction in hours or otherwise can under prevailing economic conditions, be sustained."

This inquiry promises to be of great importance for it should go to the very heart of the problem which the makers of the code had in mind when they adopted paragraph No. 2 quoted above.

It is practically the question whether an attempt to increase the purchasing power of individuals or groups by any kind of expenditures which do not produce values can increase the aggregate purchasing power of the whole population.

In view of this pending investigation we do not wish to discuss the matters at issue beyond pointing out that the policy of restricting production in the several industries with the effect of raising costs and prices without regard for the relations between the several industries tends to nullify all the benefits of improvements in industry and create an increasing scarcity of everything, and that the effects of this cannot be overcome by raising wages and prices. The average consumption of wheat in the United States is calculated to be about 4½ bushels per capita and if the total available supply should be restricted to 3½ bushels per capita no increase of either monetary stock or rates of pay would supply 4½ bushels to everybody. The pay for whatever anybody produces actually comes to him in the products of others, and if everybody restricts production in order to get an advantage in trade with his neighbors the result must be less of everything for everybody. This is really the vital question for this Inquiry to consider.

There is every reason to believe that with normal trade relations existing throughout the economic system, employment would be promptly available for every willing worker. The wants of the people are as great as ever. This country has a magnificent industrial equipment, with a capacity much beyond that of any previous time, and always increasing. It is deplorable that a people with the practical capacity of the people of the United States should stand helpless in the presence of want and distress, with the industrial organization operating far below its capacity, solely through failure to intelligently adjust the exchange relations among themselves to their mutual advantage.



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